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TREASURY FOR OFAC
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SUBJECT: CHINA SHOCKED AT E.O. 13382 DESIGNATIONS OF FOUR
CHINESE ENTITIES

REF: SECSTATE 95206

Classified By: Deputy Chief of Mission David Sedney.
Reasons 1.4 (b) and (d).

SUMMARY

11. (S) The U.S. decision to designate four Chinese companies under E.O. 13382 demonstrates that dialogue with the United States is useless, a shocked and shaken MFA Arms Control and Disarmament Director General Zhang Yan told DCM in response to ref demarche points delivered on June 13. News of the designations contradicts DG Zhang's understanding that the United States would not take E.O. action until the end of the year, which he believed was confirmed in the recent June 7 bilateral nonproliferation talks. These measures violate trust and undermine existing U.S.-China cooperation on nonproliferation and export controls. DG Zhang strongly urged the United States to stop the designations. End Summary.

12. (S) On June 13, DCM met with MFA Arms Control and Disarmament Director General Zhang Yan to deliver ref demarche points. DCM said he understood that AA/S Record had previewed with DG Zhang on the sidelines of the June 7 bilateral nonproliferation consultations in Washington the likelihood that the United States would take this action. The United States had hoped to receive additional information on the four named entities during the course of the bilateral discussions, but had not received anything from the Chinese side that would prevent the U.S. from proceeding now with the designations. The DCM said that the designations would be announced the morning of June 13 in Washington and asked that the Chinese side make no

public response before then. A shocked and shaken DG Zhang said he had no official response to the demarche points but would report the information to his superiors at a high level in the MFA.

E.O Designations Undermine Existing U.S.-PRC Cooperation

13. (S) Moving quickly to anger, DG Zhang said in his view these actions are destructive, not constructive and will undermine existing cooperation between the United States and China on nonproliferation issues. The U.S. side has not consulted with China in advance of these measures or provided any explanation of its actions, DG Zhang claimed. China has repeatedly asked the U.S. side to provide factual information about the actions of the entities but has not received information that meets any legal standard. The designations are particularly shocking considering that they come immediately after DG Zhang's June 7 bilateral consultations with AA/S Record in Washington. This demonstrates that dialogue with the United States is "useless, even hopeless." DG Zhang said he cannot accept the U.S. decision to designate the four Chinese companies and implored the DCM to immediately request that the USG stop the process of the designations and postpone the announcement. If the United States is able to provide facts against these entities, China will work to take immediate action, DG Zhang said.

DG Zhang: No Designations Until The End Of 2006

14. (S) DG Zhang said his understanding from conversations with AA/S Record during the June 7 bilateral consultations is that China had until the end of the year before the United States would designate. If the U.S. side proceeds with the designations now it will represent a violation of trust, DG Zhang said. Visibly upset, DG Zhang said "if this is U.S. diplomacy China will find other countries to engage with." DG Zhang was particularly angry that our demarche did not reference any of the progress China had shared at the June 7 talks. "If the United States was serious about non-proliferation cooperation with China," he said, "it would have recognized the major progress China is making and would cooperate for more progress." DCM pointed out that the United States had been very clear over the course of the past 10 months that designations were imminent.

The June 7 U.S.-China Bilateral Talks

15. (C) DG Zhang said he had three purposes for attending the June 7 bilateral talks in Washington: 1) to inform the U.S. side of China's "new measures and new results" in the areas of nonproliferation and export controls, 2) to enhance U.S.-China cooperation on export controls, particularly in the areas of personnel training and seminars and 3) exchange information with the United States on certain cases. China was expecting to hear additional information from the U.S. side regarding Chinese companies, but in spite of repeated requests for "new facts" or proof that these entities have engaged in any recent proliferation activities the Chinese side has yet to receive additional information. In contrast, DG Zhang said, the Chinese side has provided the United States with new information of China's efforts to tighten enforcement of export controls. Looking through his notes, DG Zhang read from the list of Chinese actions he said he had provided to the U.S. during the June 7 consultations. Information provided by DG Zhang included the following:

--The Chinese Government stopped a 10 ton shipment of sodium cyanide in 2004 destined for the DPRK. The goods were confiscated and the company was fined RMB 50,000. When the company failed to pay the fine, its assets were seized. The case has been posted on a Chinese Government website.

-- In 2005 a Chinese court sentenced one person to 9 years imprisonment with a fine of RMB 100,000 and a second person to 8 years with a fine of RMB 130,000 for attempting to smuggle a 3-axle test bench that could be used for missile tests to the DPRK. The equipment was confiscated.

--The Chinese Government stopped a Chinese company's attempt to export Zirconium powder to Iran.

--In May 2006 The State Council approved new interim administrative measures to control graphite exports.

Promulgation of the new measures is expected soon. The interim measures will apply until permanent regulations can be drafted.

--In January 2006, China implemented new measures to regulate the export of dual-use goods and technology.

--China currently is revising its nuclear-related dual-use technology export control regulations, especially the controlled items lists, to bring them into compliance with the NSG and Zanger lists.

¶6. (C) DG Zhang also said that China is doing more with regard to the DPRK and Iran, but that revealing this information could undermine China's future efforts to stop proliferation activities involving these countries.

Zhang says Designations without Basis and Counterproductive

¶7. (C) Zhang was clearly upset, angry and personally insulted by the designations. He said that the designations would undermine the Foreign Ministry's ability to work with Chinese companies, who already believed the United States would punish Chinese companies with or without evidence. Zhang returned repeatedly to the issue of legally sufficient evidence, stating that the United States had provided no legally sufficient evidence on any of the four companies that they had on-going or in the recent past had carried out illegal proliferation activities. He lashed out at what he saw as bad faith by the United States government and U.S. non-proliferation officials as untrustworthy and as not being willing or able to understand how to create cooperative relationships. DCM urged Zhang to look at the entire process over the past 10 months and to continue our positive efforts to prevent proliferation.

DG Zhang Strongly Urges USG To Stop Designations

¶8. (S) At the conclusion of the meeting, DG Zhang again reiterated China's willingness to act on "facts" the United States might provide and again strongly urged the DCM to stop the four E.O. designations scheduled for June 13. DCM responded that he would communicate DG Zhang's message back to Washington, but stressed that these actions were already in motion and that it would most likely be impossible to reverse them at this point.

¶9. (S) ACTION REQUEST: Zhang was unable to see a way forward from the designations. He would like to know how the designations once put in place can be removed. Please provide talking points on what steps China or the designated entities need to take to have the designation lifted.

RANDT

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End Cable Text